
FISCAL FOCUS

PERSONAL SERVICES CONTRACTS: AN OVERVIEW

Prepared by:
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April 1998



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TO: The Members of the House of Representatives

Personal services contracts allow individuals who are not civil servants to work for the state in a wide range of areas. State expenditures for personal services contracts increased nearly 15% from FY 1994-95 to FY 1995-96 (\$1.33 billion to \$1.52 billion, respectively). Improving state government efficiency and effectiveness, early retirement of state employees, advances in technology, and hiring limitations placed on state agencies have all contributed to the increased use of personal services contracts. Given these factors, and the variety of services state government is required to provide, the use of personal services contracts is expected to grow.

The State Constitution requires the Department of Civil Service to authorize all disbursements for personal services. Statute makes the Department of Management and Budget responsible for maintaining centralized controls over the related financial transactions. Through statutory reporting requirements, the Legislature oversees the personal services contracts process. Such a system of checks and balances is designed to ensure that contractual employees are not unnecessarily replacing classified employees and that expenditures made for such contracts do not exceed amounts authorized.

This **Fiscal Focus** provides a general overview of personal services contracts, highlights the roles played by agencies, relates actions taken in response to the Auditor General's 1996 performance audit, and explains proposed Civil Service rules changes (currently under court injunction).

Staff from the Departments of Civil Service and Management and Budget and the Office of the Auditor General reviewed the draft report; we appreciate their assistance. **Personal Services Contracts: An Overview** was prepared by Craig Thiel, Fiscal Analyst. Jeanne Dee, Administrative Assistant, assisted with graphics and formatted the report for publication.

Please call should you have questions on this report.

James J. Haag, Director

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INTRODUCTION

State government provides a myriad of services to and programs for Michigan residents. The vast majority of the time, these governmental activities are performed by employees of the classified state civil service. For a variety of reasons, however, some governmental activities may be performed by individuals working outside the civil service system. This is accomplished through a personal services contract between an operating agency and an organization or an individual who is not a classified employee.

State agencies cannot enter into personal services contracts totally unchecked. Two agencies play critical roles with respect to approving disbursements for personal services contracts and maintaining controls over related expenditures. Personal services contracts are also subject to legislative oversight. Specifically:

- The ***Department of Civil Service*** is required by the Constitution to approve or disapprove all disbursements for personal services.
- The ***Department of Management and Budget*** is responsible for establishing and maintaining centralized controls over the procurement of all goods and services, including personal services.
- The ***Legislature*** oversees personal services contracts let by executive branch operating agencies through reporting requirements contained in annual appropriation bills and/or the Management and Budget Act.

In FY 1995-96, the state expended over \$1.5 billion for personal services contracts, an increase of nearly 15% over FY 1994-95 amounts. Recently, questions have been raised by members of the Legislature over the extent and cost of personal services contracts let by the various operating agencies. In addition, members of the Legislature have given heightened attention to a June 1996

performance audit issued by the Auditor General relating to the operating and oversight roles and responsibilities of the Departments of Civil Service and Management and Budget with respect to contractual personal services.

This Fiscal Focus:

- Defines and addresses the nature of personal services contracts;
- Examines the extent of and expenditures for such contracting by state agencies over the past four-year period;
- Describes the roles and responsibilities of state agencies, with an emphasis on the roles played by the Departments of Civil Service (DCS) and Management and Budget (DMB);
- Reviews the Legislature's oversight role, focusing on various reporting requirements;
- Discusses a 1996 Auditor General performance audit; and
- Highlights the recent proposed changes to the rules/procedures governing personal services contracts and their potential impacts.

PERSONAL SERVICES CONTRACTS DEFINED

The term *personal services* generally refers to work performed for the direct benefit of the state by an individual or organization for compensation. Civil Service Commission Rule 4-6 defines a *contract for personal services* as:

"A contract between (a) an individual or organization and (b) a state agency, pursuant to which the state agency is obligated to make disbursements from appropriated funds for personal services rendered to, or for the direct benefit of, the state, by persons who are not classified employees of the state. A contract for personal services does not include a contract for the sale of both goods and services if the contract is one predominately for the sale of goods under article 2 of the uniform commercial code."

There are two distinguishing features of a personal services contract:

- A personal services contract entails a service provided by an individual, who is **not** a classified employee, for the benefit of a state agency.
- If the contract involves the procurement of both goods and services (commonly referred to as a "mixed contract"), then it is only considered a personal services contract if the following criteria apply: a) a logical and/or practical relationship between the goods and services being purchased exists and, b) the cost of the services portion exceeds the cost of the goods portion of the contract.

To illustrate this second feature, consider a mixed contract for the purchase of a new computer system and related programming services. A logical link between

the goods and services portions of the contract is present. However, if the cost of the computer equipment exceeds that of the development and programming, then the contract would be predominately for the sale of goods (i.e., computer hardware and software) and would not be considered a personal services contract. In the case of a mixed contract where a logical/practical relationship does not exist, the services portion of the contract would be separated from the goods portion and considered on its own, regardless of the cost ratio between the services and goods being purchased.

INDEPENDENT CONTRACTOR VERSUS SPECIAL PERSONAL SERVICES EMPLOYEE

State agencies acquire personal services either through an independent contractor or from a special personal services employee. After determining the need to contract for a service, the individual agency determines whether to use an independent contractor or a special personal services employee to deliver the desired service. The decision depends on a variety of criteria, such as the type of service, anticipated workload, skills required, and the anticipated duration of the service.

While the Internal Revenue Service provides an array of specific criteria to define an independent contractor,¹ the general rule is that an individual is considered an independent contractor if the employer (e.g., the state) has the right to control or direct **only** the results of the work and **not** the means and methods of accomplishing the agreed-to results. Independent contractors are generally not directly supervised by the employer and are paid on a per-job basis (as opposed to per-hour, per-week, etc.).

Independent contractors, typically, either have their own business or work for a specific business which an employer has hired to complete a task. In nearly all cases, the state contracts with an organization which then employs individuals to provide a given service. An example of a independent contractor might be Unisys, which may have been hired to provide Year 2000 programming services for a

¹ The IRS uses a list of 20 factors as the standard for determining whether an individual is an independent contractor.

department's computer systems. Contracts with independent contractors represent nearly 100% of all personal service contracts let by the state. (See **Chart 1** on page 9.)

State agencies can also procure personal services through contracts with special personal services employees. Unlike independent contractors, these employees generally work side by side with classified state employees and under the direct supervision of a state employee. They are paid for their services through the state's payroll system. In such an instance, the state enters into a contract directly with the individual providing the service, as opposed to a business or an organization which would assign specific individuals to provide the service. Expenditures for special services employees represent a very small percentage of the total expenditures for contractual personal services. (See **Chart 1** on page 9.)

APPROVALS AND EXPENDITURES

Table 1 highlights contractual personal services approval and expenditure data for the four-year period FY 1993-94 through FY 1996-97, under the current DCS rules. Prior to FY 1993-94, most operating agencies did not report expenditures by individual contract approval, instead they reported **total** expenditures for all contractual services with independent contractors. Reporting payments to special personal services employees as a separate category did not begin until FY 1993-94.

The FY 1996-97 figures in **Table 1** do not include payments for medical services to Medicaid clients which were determined to fall outside of Civil Service jurisdiction. This accounts for a decrease of approximately \$700 million in expenditures that had previously been reported as personal services by FIA. For this reason, the following analysis does not use FY 1996-97 figures for the purpose of comparison.

- During FY 1995-96, DCS approved a total of 2,455 personal services contract requests effective in FY 1995-96 and/or FY 1996-97 and beyond, a decrease of over 28% from FY 1994-95 levels.
- In FY 1995-96, total reported departmental expenditures for contractual personal services exceeded \$1.5 billion, nearly a 15% increase over FY 1994-95 levels.

The number of approvals in any given year is affected by the contracting needs of the various agencies, changes in policies on DCS jurisdiction, and increases in preauthorized contractual services over time. The increase in expenditures coupled with the decrease in approvals from FY 1994-95 to FY 1995-96 illustrates that agencies may have entered into fewer, but larger, personal services contracts

during this time period.

Together, three agencies expended over \$1.26 billion, or 83%, of the total departmental expenditures for personal services in FY 1995-96. The Family Independence Agency accounted for \$1.0 billion (65.6%), the Department of Transportation \$132.7 million (8.7%), and the Department of Community Health \$129.8 million (8.5%) of the total.

A uniform, centralized system for tracking departmental expenditures did not exist prior to FY 1997-98, and therefore it is estimated that expenditure data for this period may be under-reported. Modifications in the use of the state's accounting system, effective October 1, 1997, are intended to provide a more efficient and effective method for monitoring, controlling, and reporting expenditures.

Table 1

**SUMMARY OF CONTRACTUAL PERSONAL SERVICES APPROVALS AND EXPENDITURES
FY 1993-94 THROUGH FY 1996-97**

Fiscal Year	Total Contracts Approved ¹	Reported Departmental Expenditures		
		Independent Contractors ²	Special Personal Services Employees	Total
FY 1993-94	2,676	\$1,162,350,422	\$8,724,228	\$1,171,074,650
FY 1994-95	3,430	\$1,319,395,041	\$9,391,268	\$1,328,786,309
FY 1995-96	2,455	\$1,515,086,840	\$9,811,213	\$1,524,898,053
FY 1996-97 ³	2,820	\$779,032,294	\$11,238,750	\$790,271,044

¹Includes requests approved and effective in the current fiscal year and/or subsequent fiscal year.

² Includes expenditures for services requiring DCS approval and all preauthorized services.

³ Payments for medical services to Medicaid clients, representing approximately \$700 million in FY 1996-97, are not included.

SOURCE: Annual Contractual Services Report, Department of Civil Service

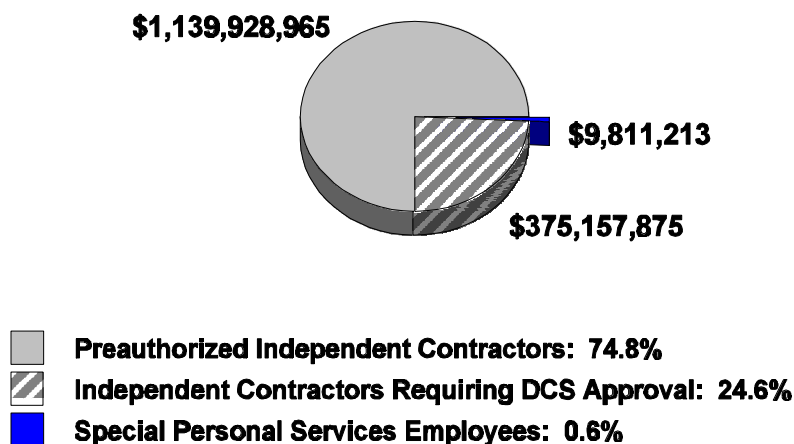
The decision to contract for personal services is driven by a number of factors, including:

- The increasing complexity of existing state services,
- Advances in information systems and technology,
- Escalating pressure to privatize certain state services,
- Full-time equated (FTE) position limitations, and
- Retirement of classified employees.

For example, the state's 1997 early retirement program resulted in over 4,900 individuals leaving the state's classified workforce. In most cases, agencies are restricted to re-filling those positions at a one-to-four ratio. It is believed that the early retirement of classified employees coupled with the rehiring restrictions placed on agencies will result in increased disbursements for personal services beginning in FY 1997-98.

Chart 1 shows that nearly 75% of the total reported expenditures for contractual personal services in FY 1995-96 were for preauthorized contracts, while just over 25% required some form of prior DCS approval. Less than 1% of the total expenditures in FY 1995-96 were for contracts with special personal services employees.

Chart 1
Contractual Personal Services Expenditures
by Contract Type



FY 1995-96 Total Expenditures: \$1,524,898,053

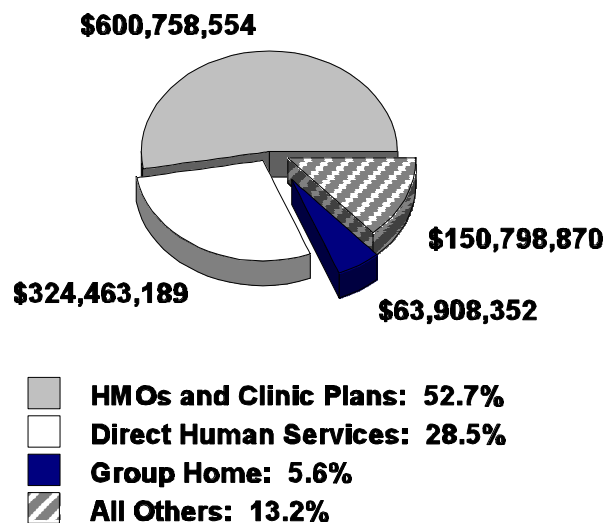
SOURCE: Annual Contractual Services Report, Department of Civil Service

The Family Independence Agency and the Department of Community Health accounted for slightly over \$1 billion, or 92%, of the total preauthorized contractual services expenditures in FY 1995-96. As **Chart 2** shows, the vast majority of the total preauthorized expenditures with independent contractors were for:

- Health care costs associated with HMOs and clinic plans (\$601 million),
- Group home services for adults and children (\$64 million), and
- Provision of direct human services, such as foster care and adoption services (\$324 million).

Chart 2

Preauthorized Contractual Expenditures



FY 1995-96 Total Expenditures: \$1,139,928,965

SOURCE: Annual Contractual Services Report, Department of Civil Service

EXECUTIVE BRANCH ROLES AND RESPONSIBILITIES

Department of Civil Service

Article 11, Section 5 of the State Constitution requires the Department of Civil Service (DCS) to approve or disapprove all disbursements for personal services. The practical implication of this constitutional requirement is that all operating agencies must obtain approval from DCS to enter into contractual arrangements involving personal services. This requirement was designed, in part, to deter operating agencies from contracting out work that can be performed by classified employees, which would circumvent the civil service system in the provision of state services.

The Department of Civil Service has jurisdiction for all disbursements for personal services **except** personal services included in mixed contracts that are predominately for the sale of goods (as measured by the cost ratio of goods to services). Therefore, only mixed contracts where the services portion outweighs the goods portion would fall under DCS jurisdiction.

Currently, there are two methods for DCS to approve agency requests to disburse funds for personal services: *prior approval* and *preauthorized approval*. It is important to note that under both methods DCS does not approve the *contracts* for personal services, but rather the Department must grant approval (in the form of authorization or preauthorization for the disbursement of funds) for contractual personal services before an agency may enter into such a contract.

Under the prior-approval process, agencies are prohibited from making disbursements for personal services in excess of \$5,000 without first obtaining

approval from DCS. A request to disburse funds for contractual personal services may be authorized only if the contract meets one or more of the following standards:

Standard A:

The services are temporary, intermittent, or irregular.

Standard B:

The services require specialized, technical, peculiar, or unique skills that are uncommon in the classified service.

Standard C:

The services require equipment that the state does not possess and the cost to obtain it would be prohibitive.

Standard D:

Obtaining the services through a contract results in significant cost savings over obtaining them in the classified service.

Generally, all disbursements above \$5,000 for personal services provided by special personal services employees must be approved under the prior-approval method regardless of the amount, type, and/or duration of service provided. This requirement is intended to prevent state agencies from filling positions with contractual employees that should be filled with classified employees. **Chart 3** illustrates the process followed by DCS and the various agencies for a request to disburse funds for contractual personal services under the prior-approval method.

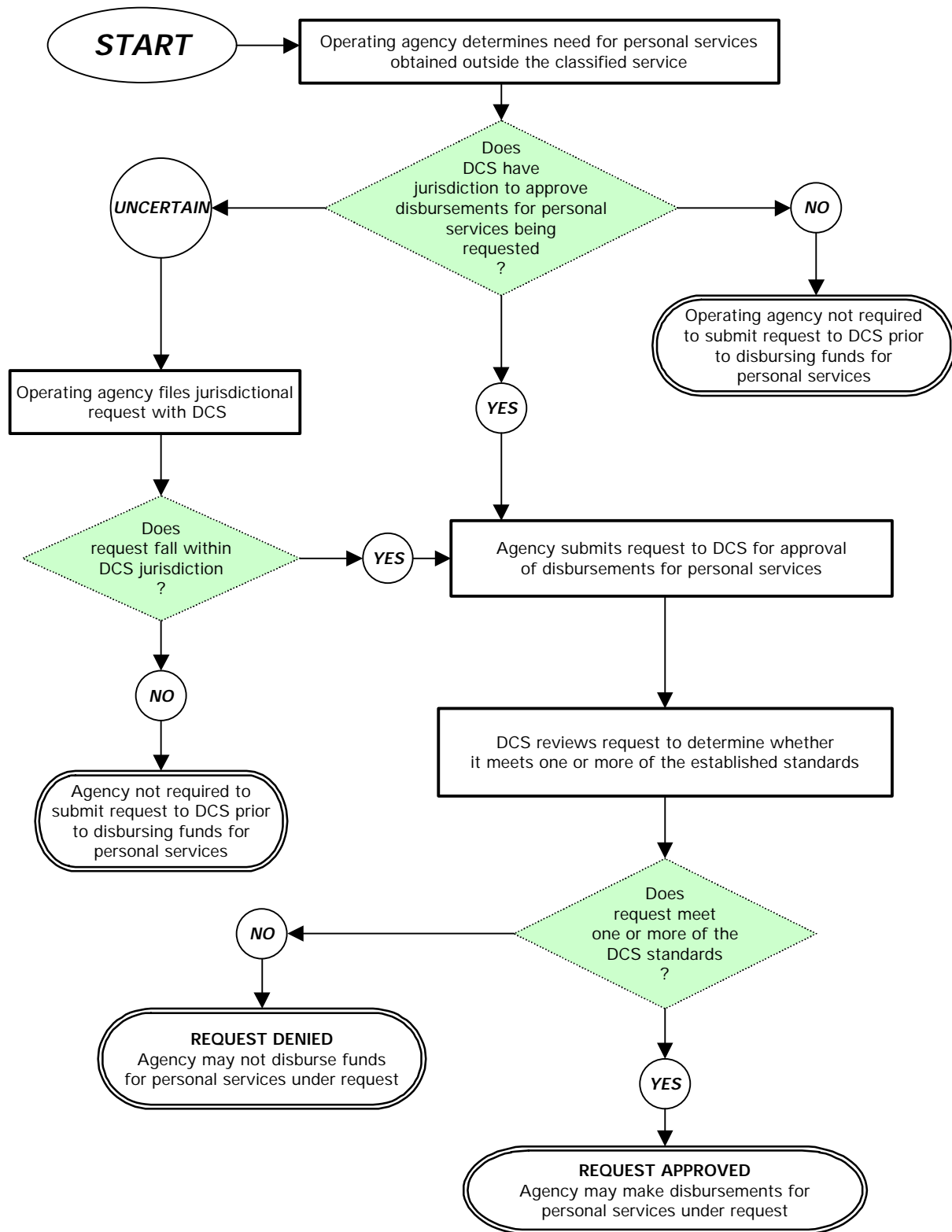
For the purpose of administrative efficiency, DCS maintains a list of preauthorized personal services deemed to meet one or more of the above standards. Preauthorized services do not require prior DCS approval for disbursement of funds, regardless of the amount. Certain services may either be preauthorized to all agencies, or preauthorized to a specific agency as the result of a formal request by that agency. For example, DCS has preauthorized such services as telephone lines and equipment services, heating and cooling services, and personnel training for all agencies. Veterinary services, on the other hand, have been preauthorized only to the Department of Agriculture as a result of a formal request.

In addition to specific preauthorized services, all contracts with independent contractors and special personal services employees that do not exceed \$5,000 in a fiscal year are preauthorized to all agencies and do not require prior DCS

approval; however, they must be reported.

Chart 3

Approval Process: Request to Disburse Funds for Contractual Personal Services



Department of Management and Budget

While DCS approves or disapproves all disbursements for personal services, the Department of Management and Budget is responsible for establishing and maintaining centralized controls over all contracts, including those for personal services. As the state's financial control agency, DMB is responsible for establishing a comprehensive system of internal controls for all state financial transactions. Therefore, it is DMB's responsibility to establish and maintain controls designed to limit contractual services expenditures to contracts that have been properly approved. The Department of Management and Budget has delegated responsibility for various types of services to the operating agencies, but still requires them to adhere to DMB policies and procedures regarding procurement.

Operating Agencies

The various operating agencies must identify the need for a service, make the initial decision whether to provide the service through the classified service or a contractor, obtain required DCS and DMB approvals, process all financial and administrative transactions for services performed, monitor the day-to-day activities of contractors, and evaluate each contractor after project completion. Generally, department staff in the areas of human resources, finance, contract administration, and/or internal audit perform these various functions. Until the 1998 fiscal year, agencies provided DCS with annual expenditure data on contractual personal services. Beginning in FY 1997-98, annual expenditure data will be available directly from the Michigan Administrative Information Network (MAIN).

LEGISLATIVE OVERSIGHT

The Legislature has maintained a long-standing oversight role in personal services contracts through reporting requirements contained in annual appropriation acts and/or the Management and Budget Act, and through performance audits conducted by the Office of the Auditor General. Prior to the 1988 amendments to the Management and Budget Act, selected annual appropriation acts contained reporting provisions pertaining to personal services contracts. These provisions, however, were not consistent in all appropriation acts, and department compliance with the provisions varied. This created discrepancies in the information provided to the Legislature.

To address the issues of uniformity and compliance with respect to reporting personal services contract information, the Management and Budget Act was amended in 1988 to require monthly and annual reports by DCS. Specifically, Section 281 of the Management and Budget Act requires that DCS provide monthly and annual reports on personal services contracts issued throughout state government to the House and Senate Appropriations Committees and to the House and Senate Fiscal Agencies. These reports detail, by agency:

- Each request to disburse funds for personal services,
- The name of the individual or contractor,
- The dollar amount and source of financing,
- The duration of the contract, and
- The expenditure information (annual report only).

It is worth noting that a uniform procedure for recording contractual expenditures in the state's accounting system did not exist until FY 1997-98, and therefore,

DCS relied on the operating agencies to provide the required expenditure data. Until recently, the DCS monthly and annual reports represented the primary mechanism by which the Legislature monitored contractual personal services and the related process.

The FY 1997-98 General Government Appropriation Act (PA 111 of 1997) contains new, additional legislative reporting requirements which were included primarily in anticipation of changes to Civil Service Rule 4-6. Effective October 1, 1997, Section 718 of PA 111 of 1997 requires monthly reports on:

- Personal services contracts awarded without competitive bidding, pricing or rate-setting;
- Personal service contracts in excess of \$100,000; and
- Any personal service contract authorizations provided to departments pursuant to delegated authority. It should be noted that this reporting requirement applies only to contracts under the proposed revisions to Rule 4-6, and therefore would not become effective until the revisions are implemented.

For each contract covered, agencies are to report the total dollar amount, the duration, vendor name, and type of service to the House and Senate Appropriations Committees and the House and Senate Fiscal Agencies. Modifications in the methods agencies use to record contractual agreements on MAIN will allow DMB to prepare and submit these new, required reports for all agencies beginning in FY 1997-98.

The 1997 early retirement program (Section 19f of PA 240 of 1943, as amended) prohibits state employees from returning to work, under contract, for the state for two years after separation from state employment. In general, this prohibition was included to prevent employees from taking advantage of the early retirement program and then returning to their positions under a personal services contract.

While this provision prohibits retired state employees from directly working for the state under contract, it does not pertain to retired employees working for temporary service agencies that may have a personal services contract with the state. For example, nothing under the 1997 early retirement program would prevent an employee from returning to work for the state under a personal services contract between a contractor, e.g., Kelly Services, and the agency where the

employee previously worked. It is unclear whether the Legislature intended that this provision address the possibility of retired employees returning to work indirectly for the state via an independent contractor after leaving state service.

In an effort to address this apparent loophole, the Legislature included language in the FY 1997-98 General Government Appropriation Act (Section 719) designed to limit the amount of time early retirees can work for a temporary service agency that is under contract with the state agency where the retired employee previously worked. Section 719 limits early retirees to 500 hours of work for professional, technical, or clerical services and 250 hours of work for management services. This limitation applies to all state agencies and only for the 24-month period after termination of employment.

The Office of the Auditor General, as part of its constitutional responsibility, also plays an important oversight role in personal services contracts through its performance audits and special reports of selected state programs. Generally, the Auditor General conducts performance audits and issues special reports to identify areas where the effectiveness and efficiency of state government can be improved. Because contractual arrangements (including those for personal services) represent an integral component of many state programs in terms of the services provided and the resources expended under contract, oversight of personal services contracts occurs on a program-by-program basis through these performance audits and special reports.

AUDITOR GENERAL PERFORMANCE AUDIT

In June 1996, the Office of the Auditor General issued a performance audit of statewide contractual personal services.² The report contains six findings and eight corresponding recommendations generally addressing DMB's and DCS's management controls, evaluations, and reporting requirements for personal services contracts. The following discussion provides a brief overview of selected audit findings, agencies' responses, and actions taken to date to address specific findings.

The Auditor General found that existing controls did not effectively limit contract expenditures to only those approved. The accompanying recommendation called for modifications to the state's accounting system to address this finding.

In response, DMB has directed agencies to record all contractual agreements (including personal services contracts) and related payments in consistent coding elements on MAIN. This change was designed to link contractual purchasing documents to payment activity in a central location. These coding requirements became effective for all new contracts beginning on or after October 1, 1997. Existing contracts were to be converted to comply with these changes by January 1, 1998; however, some exceptions to this policy have been granted.

The performance audit revealed that management controls were not sufficient to ensure compliance with DMB and DCS approval requirements. In response to this finding, DCS is requiring all agencies to use MAIN as an approval system for acquisition of all personal services provided by special personal services employees

² *Performance Audit of Statewide Contractual Personal Services: October 1, 1992 through May 31, 1995*, Office of the Auditor General, June 1996.

as well as services provided by independent contractors.

Although an electronic approval process had been available on MAIN, the new, modified electronic process replaced the paper-based system and is now the only approval option for agencies. Use of the electronic system is mandatory for all contracts effective on or after October 1, 1997. Therefore, contracts approved prior to October 1 which extend into subsequent fiscal years will require conversion.

The Auditor General report also found that DCS did not effectively monitor expenditures for personal services. The audit cited DCS for failure to compare amounts expended with approved amounts, and failure to follow up when the operating departments reported expenditures in excess of the amounts approved by DCS. The recommendation called for DCS to monitor approved expenditure data and follow up on contracts for which unapproved amounts were expended.

In response, DCS agreed to initiate a post-audit process beginning with data submitted by agencies for the FY 1994-95 annual report. The requirement for agencies to record all contractual agreements and subsequent payments on MAIN should allow DCS to more effectively monitor expenditures, and it will obviate the need to rely solely on agencies to self-report this data.

Another performance audit finding was that agencies were not adequately monitoring contractor progress or evaluating contractor effectiveness at completion of the project. Although the recommendation directly cites weaknesses in the agencies' controls, DMB has the responsibility of overall contract monitoring for the state. To address this finding, DMB has indicated its intent to work with agencies to enhance their contract monitoring skills. The Department of Management and Budget also plans to encourage all agency internal auditors to play a more active role in contract monitoring and evaluation compliance.

The changes were made with the intent of providing DCS and DMB with more accurate information to meet legislative reporting requirements and to compile the required monthly and annual reports. While actions have been taken by DCS and DMB on various fronts to address findings contained in the performance audit, the efficacy of the changes and modifications will not be known until the Auditor General reviews the revised processes.

CIVIL SERVICE RULE CHANGES

On May 8, 1997, the Civil Service Commission approved significant revisions to Rule 4-6 which effectively change the roles and responsibilities of DCS and the various operating agencies relating to disbursements for personal services. However, the revised rule is currently under a court injunction³ and until the legal challenge is resolved, operating agencies and DCS will continue to operate under the 1993 version of Rule 4-6. While the revisions are designed to streamline and expedite the personal services approval process for agencies and DCS, they have the potential to adversely affect oversight of the process.

Probably the most significant and controversial change associated with the revisions to Rule 4-6 is establishment of a third method by which DCS can approve disbursements for personal services. This revised rule provides a *decentralized approval* procedure. The decentralized method allows an agency, if it meets DCS standards (e.g., training, documentation, record keeping, and notification), to self-approve disbursements for personal services, subject to later audit by DCS staff. Agencies may self-approve disbursements for personal services by independent contractors provided the contract does **not**:

- Result in a layoff or demotion of a classified employee,
- Exceed \$500,000 in any one year or \$2 million over its life, or
- Result in six or more similar contracts.

If any of these criteria are met, the agency must file a request and obtain prior DCS approval. Disbursements for contracts with special personal services employees cannot be approved under the decentralized procedure; these contracts

³ The revisions to Rule 4-6, approved on May 8, 1997, became effective June 2; however, on June 10, Ingham County Circuit Court Judge James R. Giddings issued a preliminary injunction to suspend implementation of the revisions.

continue to require prior DCS approval.

The decentralized method effectively provides agencies with more authority for disbursements for personal services, as the requirement for prior DCS approval for the vast majority of contracts is eliminated. Ultimately, under the revisions to Rule 4-6, DCS will be reviewing far fewer requests for disbursements and, therefore, will have a diminished role in the oversight of personal service contracts. To the extent that these changes reduce the scope of DCS's monthly and annual reporting required under the Management and Budget Act, the Legislature's oversight role could be weakened.

Table 2 highlights major changes between the 1993 and 1997 versions of Rule 4-6 regarding disbursements for personal services.

Table 2

CHANGES BETWEEN 1993 AND 1997 VERSIONS OF RULE 4-6 REGARDING DISBURSEMENTS FOR PERSONAL SERVICES

	1993 Rule	1997 Rule
What is the extent of DCS jurisdiction?	Jurisdiction over all disbursements for personal services <i>except</i> those included in contracts predominately for the sale of goods (i.e., mixed contract)	Jurisdiction over <i>all</i> disbursements for personal services
What are the methods available for DCS to approve agency requests to make disbursements for personal services?	Prior Approval: agency must obtain DCS staff approval to make disbursements Preauthorized Approval: DCS maintains list of pre-authorized services (meeting one or more of the DCS standards)	Same as 1993 rule, plus Decentralized Approval: agency also permitted to self-approve a request if it meets DCS standards, subject to later audit by DCS staff
Are contracts with special personal services (SPS) employees treated differently than contracts with independent contractors?	No	Yes: 1) SPS contracts cannot be approved under the new decentralized procedure 2) SPS contracts can be approved only under Standard A or Standard B
What are the standards available to the DCS for approving disbursements for personal services?	Standard A: Temporary, intermittent, or irregular personal services Standard B: Uncommon personal services Standard C: Lack of equipment or materials Standard D: Substantial cost savings	For independent contracts, same as 1993 Standards A through D plus Standard E: Included in contract with predominant purpose other than personal services For SPS employees, only Standard A and Standard B of 1993 rule
When can an agency self-approve disbursements for personal services under the decentralized procedure?	Self-approval option not available	An agency can self-approve for all personal services by independent contractors except when the contract: 1) Results in a layoff or demotion of a classified employee, 2) Exceeds \$500,000 in any one year or \$2 million over the life of the contract, or 3) Is similar to six or more similar contracts
How are "mixed contracts" (contracts that authorize disbursements for both personal services and goods) treated?	DCS has no jurisdiction over any personal services included in a contract that is predominately for something other than personal services	Under 1997 Standard E , DCS may permit disbursements for personal services based on the fact that they are part of a contract that is predominately for something other than personal services

SOURCE: Department of Civil Service

STATEWIDE CONTRACTING POLICY AND PROCEDURAL CHANGES

In addition to revisions to Rule 4-6, DCS and DMB have implemented new policies and procedures regarding all state contractual agreements, including personal services contracts, effective October 1, 1997. These changes are designed to enhance the state's overall contract management capabilities including approving, monitoring, and reporting functions. They were implemented partially in response to new legislative reporting requirements contained in the FY 1997-98 General Government Appropriation Act.

Uniform Coding Elements

Agencies have been directed by DMB and DCS to use uniform coding elements to record all contractual agreements (including those for personal services) and related payments in the state's purchasing and accounting systems. For most agencies, this represents a new use of MAIN, and subsequently addresses a major finding of the 1996 Auditor General performance audit. Using MAIN in this manner will allow agencies to track all expenditures associated with a specific contract. Legislative requests for information regarding contracts let by an agency should benefit from this added functionality.

Electronic Requests to Disburse Funds

Agencies have also been instructed to use MAIN for submitting requests to disburse funds for personal services—replacing the previous paper-based system. This change is designed to automate and streamline the approval process and reduce the paper record-keeping responsibilities of agencies and DCS. Furthermore, an electronic approval system will facilitate tracking individual requests through the system.

The new policy requiring uniform coding of all contractual agreements and

payments in MAIN will allow DCS and DMB to better monitor expenditure activity and prepare and submit all required reports. These enhancements should improve the accuracy of reports submitted to the Legislature, especially with respect to personal services expenditure data.

It is still too early to ascertain the specific impact that various policy/procedural changes have had on the state's overall contract management capabilities. However, the efficacy of these changes should be reflected in future Auditor General performance audits.

With specific respect to personal services contracts, these policy changes have allowed DMB to meet the new monthly legislative reporting requirements, which, in turn, enhances the Legislature's ability to exercise its oversight role. Any additional modifications necessary to ensure an accurate, timely, and effective contract management system will be addressed throughout the year.

CONCLUSION

Legislative oversight of personal services contracts is currently maintained primarily through monthly and yearly reporting by DMB and DCS. Recently, the Legislature has taken an active role to ensure that current reporting requirements are modified to address changes in civil service rules/procedures, the state's early retirement program, and the changing nature of state contracting.

It is likely that there will be continued enhancements to the Legislature's oversight role through the appropriation process and other venues. In addition, the Legislature may wish to consider reevaluating reporting requirements under the Management and Budget Act in light of recent changes in the personal services contract procedures, modifications to agencies' use of MAIN, and the state's overall contract management responsibilities.

Legislative oversight will also be enhanced by the efforts of operating agencies to improve their overall contract management activities. Monitoring contractor progress through periodic reports and evaluating contractor performance via final evaluations may become some of the basic oversight responsibilities of all agencies. Agency internal auditors are also in the position to track contract expenditures to ensure they do not exceed approved amounts and to report, in a timely manner, any discrepancies to the chief financial officer or equivalent.

State agencies' use of contractual personal services will continue as long as state government provides the vast array of services required by state law. An effective system of checks and balances for contractual personal services (involving both the legislative and executive branches of state government) will ensure that contractual employees are not unnecessarily replacing classified employees and that expenditures made for such contracts do not exceed amounts authorized.

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